FILED
DEC 20 1991
OFFICE OF THE CLERK

No. 91-42

IN THE

Supreme Court of the United States

OCTOBER TERM, 1991

UNITED STATES OF AMERICA,

Petitioner,

—v.—

THERESE A. BURKE, *et al.*,

Respondents.

ON WRIT OF *CERTIORARI* TO THE
UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF *AMICUS CURIAE* OF THE AMERICAN CIVIL LIBERTIES UNION, NOW LEGAL DEFENSE AND EDUCATION FUND, AND NAACP LEGAL DEFENSE AND EDUCATIONAL FUND, IN SUPPORT OF RESPONDENTS

Steven R. Shapiro
Isabelle Katz Pinzler
American Civil Liberties Union
Foundation
132 West 43 Street
New York, New York 10036
(212) 944-9800

Julius L. Chambers
Charles Stephen Ralston
NAACP Legal Defense and
Educational Fund, Inc.
99 Hudson Street
New York, New York 10013
(212) 219-1900

C. Cabell Chinnis, Jr.
(*Counsel of Record*)
Elahna R. Strom
Philip L. Gordon
Elizabeth B. Dixon
Julie E. Barland
Latham & Watkins
1001 Pennsylvania Avenue, N.W.
Washington, D.C. 20004
(202) 637-2200

Alison C. Wetherfield
Martha F. Davis
NOW Legal Defense and
Education Fund
99 Hudson Street
New York, New York 10013
(212) 925-6635

BEST AVAILABLE COPY

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES iv

INTEREST OF *AMICI CURIAE* 1

SUMMARY OF ARGUMENT 2

ARGUMENT 4

I. For over seventy years Congress and the courts have excluded from gross income damages received on account of any personal injury, including both physical and nonphysical injuries. The Commissioner adds into section 104(a)(2) a distinction between physical and nonphysical injuries that conflicts with the plain terms of the statute, has no legislative or judicial support, and is logically flawed. 4

A. The Commissioner's distinction between physical and nonphysical injuries conflicts with the plain terms of the statute and creates a restriction on section 104 (a)(2) that Congress considered and rejected. 6

B. The distinction between physical and nonphysical injuries has been rejected by five Courts of Appeals and the Tax Court. . . 7

C. The Commissioner's proposed distinction leads to capricious results. 8

D. There is no logical means to distinguish between physical and nonphysical injuries. . . 9

Page

E. The inexorable consequence of the Commissioner's test is taxation of damages for physical injuries. 10

II. In applying section 104(a)(2), the Courts of Appeals and the Tax Court have looked to the nature of the claim asserted by the victim. They have made no distinction between economic and noneconomic damages from personal injuries. 12

A. The Courts of Appeals and the Tax Court have concluded that a "nature of the claim" test implements the intent of section 104(a)(2). 13

B. The Commissioner's proposed test is at odds with the statute and this Court's precepts in *Woodward* and *Gilmore*, and is based on an inapplicable theory regarding the taxation of damages. 16

III. The Commissioner's proposed approach, in which damages attributable to a nonphysical injury are excludable only where they *restore lost capital*, is conceptually misguided, is contrary to the statute, and renders section 104(a)(2) superfluous. 18

A. The Commissioner's definition of "personal capital" is conceptually misguided. 19

B. The Commissioner's proposed test has no basis in the statute. 21

C. The Commissioner's argument renders section 104(a)(2) superfluous. 22

Page

D. The Commissioner's test relies on a theory that has no discernable scope. 23

IV. Amounts received by respondents in settlement of their Title VII suit are excludable from income under section 104(a)(2). 24

A. A violation of Title VII results in "personal injuries" within the meaning of section 104(a)(2). 24

B. Title VII back pay awards are damages within the meaning of section 104(a)(2). 27

CONCLUSION 28

TABLE OF AUTHORITIES

Page

CASES

Bent v. Commissioner, 835 F.2d 67 (3d Cir. 1987) . . . *passim*
Bernier v. Bernier, 147 U.S. 242 (1893) 22
Brooms v. Regal Tube Co., 881 F.2d 412 (7th Cir. 1989) 26
Byrne v. Commissioner, 883 F.2d 211 (3d Cir. 1989) 17, 25
Church v. Commissioner, 80 T.C. 1104 (1983) 8, 18
Commissioner v. Glenshaw Glass Co., 348 U.S. 426 (1955) 4, 21, 22, 23
Commissioner v. Miller, 914 F.2d 586 (4th Cir. 1990) 8
Crane v. Commissioner, 331 U.S. 1 (1947) 6
Curtis v. Loether, 415 U.S. 189 (1974) 25
Downey v. Commissioner, 97 T.C. 150 (1991) 18
Doyle v. Mitchell Bros. Co., 247 U.S. 179 (1918) 22
Escondido Mutual Water Co. v. LaJolla Band of Mission Indians, 466 U.S. 765 (1984) 28
Glynn v. Commissioner, 76 T.C. 116 (1981) 24
Goodman v. Lukens Steel Co., 482 U.S. 656 (1987) . . . 25, 26
Hawkins v. Commissioner, 6 B.T.A. 1023 (1927) . . 10, 20, 23
James v. United States, 760 F.2d 590 (5th Cir. 1985) 16
McDonald v. Commissioner, 9 B.T.A. 1340 (1928) 16, 23
Metzger v. Commissioner, 88 T.C. 834 (1987), *aff'd without opinion*, 845 F.2d 1013 (3d Cir. 1988) 15, 26
National-Standard Co. v. Commissioner, 749 F.2d 369 (6th Cir. 1984) 4
Owens v. Okure, 488 U.S. 235 (1989) 26
Pistillo v. Commissioner, 912 F.2d 145 (6th Cir. 1990) . . . . . *passim*
Price Waterhouse v. Hopkins, 490 U.S. 228 (1989) 25
Redfield v. Insurance Co. of N. Am., 940 F.2d 542 (9th Cir. 1991) 13

Page

Rickel v. Commissioner, 900 F.2d 655 (3d Cir. 1990) 8, 17, 24, 25
Roemer v. Commissioner, 716 F.2d 693 (9th Cir. 1983) . . . . . *passim*
Singer v. United States, 323 U.S. 338 (1945) 22
Sparrow v. Commissioner, 1991 U.S. App. LEXIS 27991 (D.C. Cir. Nov. 26, 1991) 27
Thompson v. Commissioner, 866 F.2d 709 (4th Cir. 1989) . . . . . *passim*
Threlkeld v. Commissioner, 87 T.C. 1294 (1986), *aff'd*, 848 F.2d 81 (6th Cir. 1988) . . . . . *passim*
Threlkeld v. Commissioner, 848 F.2d 81 (6th Cir. 1988) 7, 13, 15
United States v. Garber, 589 F.2d 843 (5th Cir.), *rev'd*, 607 F.2d 92 (5th Cir. 1979) 10
United States v. Gilmore, 372 U.S. 39 (1963) . . . . . *passim*
United States v. James, 478 U.S. 597 (1986) 16
United States v. Kaiser, 363 U.S. 299 (1960) 20
Woodward v. Commissioner, 397 U.S. 572 (1970) . . 14, 15, 16
Wulf v. City of Wichita, 883 F.2d 842 (10th Cir. 1989) 7, 13, 17, 25
Zabkowicz v. West Bend Co., 789 F.2d 540 (7th Cir. 1986) 26

STATUTES AND REGULATIONS

42 U.S.C. § 1981 (1988) 25, 26, 27
42 U.S.C. § 1983 (1988) 25, 26, 27
Civil Rights Act of 1964, Tit. VII, 42 U.S.C. § 2000e *et seq.* (1988) . . . . . *passim*
I.R.C. (26 U.S.C.) § 61(a) 4
I.R.C. (26 U.S.C.) § 104(a) 5, 7, 27
I.R.C. (26 U.S.C.) § 104(a)(1) 27
I.R.C. (26 U.S.C.) § 104(a)(2) . . . . . *passim*
I.R.C. (26 U.S.C.) § 104(a)(3) 27
I.R.C. (26 U.S.C.) § 104(a)(4) 27

Page

I.R.C. (26 U.S.C.) § 104(a)(5) 27
I.R.C. (26 U.S.C.) § 6305(b) 28
Omnibus Budget Reconciliation Act of 1989, Pub. L. No. 101-239, § 7641(a), 103 Stat. 2106 (1989) (codified at 26 U.S.C. § 104 (Supp. I 1989)) 7
Revenue Act of 1918, Pub. L. No. 65-254, ch. 18, § 213(b)(6), 40 Stat. 1057 5
Treas. Reg. § 1.104-1(c) 4, 27

OTHER AUTHORITIES

31 Op. Att'y Gen. 304 (1918) 10, 20, 22, 23
Black's Law Dictionary (5th ed. 1979) 25, 27
Boris I. Bittker & Martin J. McMahon, Jr., Federal Income Taxation of Individuals (1988) 21
Fouts, *Payments Received in Settlement of Litigation and Claims*, 25 N.Y.U. Inst. Fed. Txn. 555 (1966) 18
H.R. Rep. No. 767, 65th Cong., 2d Sess. (1918) 5
H.R. Rep. No. 40, 102d Cong., 1st Sess., pt. 1 (1991) 26
H.R. Rep. No. 247, 101st Cong., 1st Sess., *reprinted in* 1989 U.S.C.C.A.N. 2824 7
Knickerbocker, *The Income Tax Treatment of Damages: A Study in the Difficulties of the Income Concept*, 47 Cornell L.Q. 429 (1962) 11
Rev. Rul. 56-518, 1956-2 C.B. 25 8
Rev. Rul. 61-1, 1961-1 C.B. 14 . . . . . 11, 16, 20
Rev. Rul. 72-341, 1972-2 C.B. 32 9
Rev. Rul. 85-98, 1985-2 C.B. 51 8
Rev. Rul. 85-143, 1985-2 C.B. 55 . . . . . 8, 20
William Shakespeare, *Othello*, act 4, sc. 2 19
Sol. Op. 132, I-1 C.B. 92 (1922) 12, 20, 22, 23
Sol. Op. 1384, 2 C.B. 71 (1920) 10, 20

INTEREST OF *AMICI CURIAE*[1]

The American Civil Liberties Union ("ACLU") is a nationwide, nonpartisan organization of almost 300,000 members, dedicated to protecting fundamental rights, including the right to equal treatment under the law. The ACLU has established the Women's Rights Project to work towards the elimination of the pervasive problem of gender-based discrimination. It is also involved in challenges to many other forms of discrimination including discrimination based on race, national origin, religion and disability. The ACLU has participated, both directly and as *amicus curiae*, in the litigation of many cases before the Supreme Court and other courts challenging various discriminatory practices. It submits this brief to support the proposition that victims of discrimination, like victims of other forms of wrongful conduct, should not be required to pay taxes on amounts recovered for violations of their legal rights.

The NAACP Legal Defense and Educational Fund, Inc., is a nonprofit corporation organized under the laws of the State of New York as a legal aid society. It was formed to assist African Americans to secure their constitutional and civil rights through the courts. For many years, its attorneys have represented parties and appeared as *amicus curiae* in this Court and in the lower federal courts on a broad range of issues, including both the substantive and procedural law relevant to cases of racial discrimination. It submits this brief because, if the government's position is sustained in the present case, the effectiveness of the remedies for discrimination will be significantly diminished and the burdens imposed on employers and employees by treating awards as taxable income will make settlement more difficult.

The NOW Legal Defense and Education Fund ("NOW LDEF") was established as a nonprofit women's rights law center in 1970 by founders of the National Organization for Women, and since that time has consistently worked on

---

1. Letters of consent to the filing of this brief have been lodged with the Clerk of the Court pursuant to Supreme Court Rule 37.3.

important legal cases and in advocacy and public education concerning the rights of women. NOW LDEF has particular concern for discrimination against women in the workplace, and supports efforts to address the injuries arising from such discrimination. Consistent with these efforts, it submits this brief.

SUMMARY OF ARGUMENT

Since 1918, under what is now I.R.C. § 104(a)(2),[2] Congress has excluded from gross income "any damages" that are received on account of a "personal injury." This exclusion has applied without regard to whether the injury is physical or nonphysical, and the courts and the Commissioner have uniformly so held.

Consistent with the terms of the statute and this Court's holding in *United States v. Gilmore*, 372 U.S. 39, 44 (1963), the Courts of Appeals and the Tax Court have unanimously looked to the "nature of the *claim*" to determine the applicability of § 104(a)(2). The nature of the *damages* is irrelevant. Once a victim has suffered a personal injury, § 104(a)(2) excludes from gross income all damages for both economic consequences (*e.g.*, lost wages) and noneconomic consequences (*e.g.*, pain and suffering). In accord with this test, four Courts of Appeals have held that recoveries for discrimination under Title VII of the Civil Rights Act of 1964, 42 U.S.C. § 2000e *et seq.* (1988), and other anti-discrimination statutes constitute damages received on account of a personal injury. The "nature of the claim" test is consistent with this Court's precedent and is analytically sound. It should be upheld.

The Commissioner would have this Court establish a different standard. First, the Commissioner urges that § 104(a)(2) should be read to divide personal injuries into "physical" and "nonphysical" injuries. Second, the Commissioner has proposed that § 104(a)(2) should exclude from gross income recoveries for nonphysical injuries only to the extent they constitute a "return of capital."

This Court should reject the Commissioner's interpretation of § 104(a)(2). The separation of physical and nonphysical injuries conflicts with the clear terms of the statute, which make no distinction between physical and nonphysical injuries. Moreover, this proposed distinction has been expressly rejected by Congress, leads to capricious results, has been rejected by five Courts of Appeals and the Tax Court, and would inevitably lead to the taxation of damages for physical injuries as well.

The Commissioner's second proposal should also be rejected because it, too, is at odds with the clear language of the statute itself and suffers from several additional flaws. First, the Commissioner's proposed test fails to recognize that attributes such as integrity, self-respect, and dignity are as much a part of "human capital" as are arms and legs. Second, the test is without basis in the Tax Code and is technically and logically flawed. Third, the Commissioner's test would render § 104(a)(2) superfluous for nonphysical injuries: If § 104(a)(2) applied only to a "return of capital," the provision would serve no purpose because a "return of capital" does not constitute income. Finally, this additional test relies upon a confusing theory of return of human capital that is of uncertain scope and application.

For all of the above reasons, the arguments offered by the Commissioner should be rejected. The judgment of the Court of Appeals should be affirmed.

---

2. Internal Revenue Code (26 U.S.C.) § 104(a)(2) (hereinafter I.R.C. or the Code).

ARGUMENT

I. For over seventy years Congress and the courts have excluded from gross income damages received on account of any personal injury, including both physical and nonphysical injuries. The Commissioner adds into section 104(a)(2) a distinction between physical and nonphysical injuries that conflicts with the plain terms of the statute, has no legislative or judicial support, and is logically flawed.

Section 61(a) of the Code, which is the statutory starting point for a determination of gross income, provides that, except as otherwise stated in the Code, gross income includes "all income from whatever source derived." All accessions to wealth realized by a taxpayer are therefore presumed to be gross income and taxable, unless the taxpayer can demonstrate that an accession fits into one of the specific exclusions created elsewhere in the Code. *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 430 (1955) (Congress intended to tax all gains except those specifically exempted).[3] One such exclusion is codified at I.R.C. § 104(a)(2), which states:

> [G]ross income does not include . . . (2) the amount of any damages received (whether by suit or agreement and whether as lump sums or as periodic payments) on account of personal injuries or sickness . . . .

In interpretation of the statute, Treas. Reg. § 1.104-1(c) further provides: "The term 'damages received (whether by suit or agreement)' means an amount received (other than workmen's compensation) through prosecution of a legal suit or action based upon tort or tort-type rights, or through a settlement

3. The parties have apparently agreed that the award represents an "accession to wealth." *See* Brief for the United States at 9 (hereinafter SG Brief). This determination, however, is a question of law subject to *de novo* review by this Court. *See Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 429 (1955); *see also National-Standard Co. v. Commissioner*, 749 F.2d 369, 371 (6th Cir. 1984).

agreement entered into in lieu of such prosecution." An examination of the statute itself, the circumstances surrounding its enactment, and subsequent judicial interpretations demonstrates that Congress intended to exclude from income all damages, including back pay, received on account of any personal injury, including nonphysical injuries such as discrimination.

In 1918, Congress enacted the legislative predecessor of what is now § 104(a)(2). Although Congress apparently shared the then-widespread belief that damages received on account of personal injuries were not even within the Sixteenth Amendment's definition of income,[4] Congress wished to ensure that victims of personal injury would receive any recoveries for the injury free of taxation. Accordingly, § 213(b)(6) of the Revenue Act of 1918 excluded from gross income the following:

> Amounts received, through accident or health insurance or under workmen's compensation acts, as compensation for personal injuries or sickness, plus the amount of any damages received whether by suit or agreement on account of such injuries or sickness.

Revenue Act of 1918, Pub. L. No. 65-254, ch. 18, § 213(b)(6), 40 Stat. 1057, 1065-66. The provision has continued to the present with only minor modifications.[5] It currently excludes

4. The legislative history of the Revenue Act of 1918 reflects this belief:

> Under the present law it is doubtful whether amounts received through accident or health insurance, or under workmen's compensation acts, as compensation for personal injury or sickness, and damages received on account of such injuries or sickness, are required to be included in gross income.

H.R. Rep. No. 767, 65th Cong., 2d Sess. 9-10 (1918).

5. In its rearrangement of existing law in 1954, Congress chose to separate the provisions relating to the exclusion for workmen's compensation payments, accident and health insurance proceeds, and damages for personal injury recoveries. *See* I.R.C. § 104(a). The regulations follow this division. This isolation of "personal injury" from other recoveries, such as accident and

(continued...)

from gross income "the amount of any damages received . . . on account of personal injuries or sickness." I.R.C. § 104(a)(2).

Since its inception in 1918, § 104(a)(2) has therefore excluded from gross income all damages received by a victim of a personal injury on account of that injury. The provision has never contained any distinction between physical and nonphysical injuries.

A. The Commissioner's distinction between physical and nonphysical injuries conflicts with the plain terms of the statute and creates a restriction on section 104(a)(2) that Congress considered and rejected.

Despite the clear terms of the statute excluding damages for "personal injury" without regard to physical or nonphysical injuries, the Commissioner proposes a test that would accord different treatment to damages depending upon whether those damages were received on account of a physical personal injury or a nonphysical personal injury. SG Brief at 14, 20-21. It is well-settled that "the words of statutes -- including revenue acts -- should be interpreted where possible in their ordinary, everyday senses." *Crane v. Commissioner*, 331 U.S. 1, 6 (1947). As three Courts of Appeals have noted in this context: "The ordinary meaning of a personal injury is not limited to a physical one." *Roemer v. Commissioner*, 716 F.2d 693, 697 (9th Cir. 1983).[6]

Moreover, the Commissioner's distinction between physical and nonphysical injury was recently considered and rejected by Congress. In 1989, the House of Representatives

---

5.(...continued)
health insurance proceeds, provides further support that Congress believed that personal injuries may be more than purely physical.

6. This passage is quoted with approval in *Bent v. Commissioner*, 835 F.2d 67, 70 (3d Cir. 1987). *See Pistillo v. Commissioner*, 912 F.2d 145, 148 (6th Cir. 1990) ("the meaning of 'personal injuries' encompasses both physical and nonphysical injuries").

approved a provision that would have limited the exclusion of § 104(a)(2) to amounts received on account of physical injury. The proposal was intended to reverse recent court decisions broadly interpreting § 104(a)(2) "to cover awards for personal injury that do not relate to a physical injury," such as "cases involving employment discrimination and injury to reputation where there is no physical injury or sickness." H.R. Rep. No. 247, 101st Cong., 1st Sess. 1354-55, *reprinted in* 1989 U.S.C.C.A.N. 2824-25. At the time of the proposal, four Courts of Appeals and the Tax Court had interpreted § 104(a)(2) to exclude from gross income all damages received on account of a nonphysical personal injury, such as employment discrimination or defamation.[7]

The Conferees rejected the House proposal and refused to limit the exclusion in § 104(a)(2) to recoveries for physical injuries. Instead, Congress passed a much narrower provision that limited the scope of the exclusion for punitive damages. Under this provision, punitive damages from a nonphysical injury are now outside the scope of § 104(a).[8] Section 104(a) remained unaltered in all other respects.

B. The distinction between physical and nonphysical injuries has been rejected by five Courts of Appeals and the Tax Court.

The Commissioner's interpretation conflicts with the unanimous holdings of five Circuit Courts and the Tax Court. The Third, Fourth, Sixth, Ninth, and Tenth Circuit Courts of Appeals have determined that § 104(a)(2) covers damages from both physical and nonphysical injuries in equal measure.

---

7. *See Wulf v. City of Wichita*, 883 F.2d 842 (10th Cir. 1989); *Thompson v. Commissioner*, 866 F.2d 709 (4th Cir. 1989); *Threlkeld v. Commissioner*, 848 F.2d 81 (6th Cir. 1988), *aff'g* 87 T.C. 1295 (1986); *Bent*, 835 F.2d 637; *Roemer v. Commissioner*, 716 F.2d 693 (9th Cir. 1983).

8. *See* Omnibus Budget Reconciliation Act of 1989, Pub. L. No. 101-239, § 7641(a), 103 Stat. 2106, 2379 (1989) (codified at 26 U.S.C. § 104 (Supp. I 1989)).

Commissioner v. Miller, 914 F.2d 586, 589 (4th Cir. 1990) (defamation action is action for personal injuries); *Pistillo v. Commissioner*, 912 F.2d 145, 148 (6th Cir. 1990) ("the meaning of 'personal injuries' encompasses both physical and nonphysical injuries"); *Rickel v. Commissioner*, 900 F.2d 655, 658 (3d Cir. 1990) ("personal injuries" under § 104(a)(2) encompass both physical and nonphysical injuries); *Thompson v. Commissioner*, 866 F.2d 709, 711 (4th Cir. 1989) ("relevant distinction [is] . . . not between physical and nonphysical injuries"); *Bent v. Commissioner*, 835 F.2d 67, 70 (3d Cir. 1987) ("ordinary meaning" of personal injury includes both physical and nonphysical injuries); *Roemer*, 716 F.2d at 697 (finding "ordinary meaning" of personal injury to include both physical and nonphysical injuries); *Threlkeld v. Commissioner*, 87 T.C. 1294, 1297 (1986) ("[n]o distinction is made between physical and nonphysical . . . injuries"), *aff'd*, 848 F.2d 81 (6th Cir. 1988). Even the Commissioner has ruled that compensation for lost income received on account of a nonphysical injury is not taxable income. *See* Rev. Rul. 85-143, 1985-2 C.B. 55; Rev. Rul. 85-98, 1985-2 C.B. 51 (both holding that nonphysical injuries are within the scope of § 104(a)(2)); Rev. Rul. 56-518, 1956-2 C.B. 25 ("damage to . . . professional or economic advancement" from Nazi persecution not taxable).

Not a single court has advanced any distinction between physical and nonphysical injuries in determining the scope of § 104(a)(2) and its predecessors. The courts have specifically declined to do so when urged by the Commissioner. *See, e.g., Bent*, 835 F.2d at 70; *Church v. Commissioner*, 80 T.C. 1104, 1106 (1983). This Court should not impose such a distinction now.

C. The Commissioner's proposed distinction leads to capricious results.

The distinction between physical and nonphysical injuries results in disparate treatment of similarly situated taxpayers under § 104(a)(2). As the Tax Court noted in its *en banc*

opinion[9] in *Threlkeld*, if a tortfeasor causes a surgeon to lose a finger, the loss will cause both noneconomic consequences (*e.g.*, pain and suffering) and economic consequences (*e.g.*, lost income). The entire amount of damages received is excludable. 87 T.C. at 1300. If the surgeon's injuries were nonphysical (*e.g.*, defamation), the Commissioner would require that courts "delve[] into an inquiry regarding the nature of the consequences of the injury," *id.* at 1300-01, to determine which portion of the award represented a recovery for economic consequences and which portion represented a recovery for noneconomic consequences. For nonphysical injuries, the Commissioner would tax the recovery for economic consequences as an accession to wealth: The lost income would have been taxable when earned. SG Brief at 21. *See* Rev. Rul. 72-341, 1972-2 C.B. 32. There is no logical basis for this distinction between these two tort victims, and this Court should not accept it. There is no reason to believe that Congress intended such inconsistencies. "We should be slow to attribute to Congress a purpose producing such unequal treatment among taxpayers, resting on no rational foundation." *Gilmore*, 372 U.S. at 48.

D. There is no logical means to distinguish between physical and nonphysical injuries.

The Commissioner's distinction between physical and nonphysical injuries is semantic and arbitrary. No principle of taxation provides any guidance for differentiating between recoveries for physical and nonphysical injuries.

The practical problems of the Commissioner's proposed test are immediately apparent. A taxpayer whose back is broken suffers both broken bones and mental pain and suffering. He may also suffer a loss of wages if he is subsequently fired from his job. The Commissioner's test would require courts to determine whether the firing took place as a result of the physical injury (impaired mobility) or the

---

9. Technically, the Tax Court does not sit *en banc* but rather reviews certain decisions as a "Full Court."

nonphysical injury (depression and anxiety). Similarly, a victim of discrimination on the job may suffer both an affront to her dignitary interests and headaches, ulcers, as well as other ailments. It becomes impossible as a practical matter to differentiate the harm from the effect on the tort victim.

There is no principle of taxation that would enable courts to make the distinctions in the Commissioner's proposed test. Both an arm and intellect, for example, constitute human capital. *See Hawkins v. Commissioner*, 6 B.T.A. 1023, 1025 (1927) (reputation as human capital); 31 Op. Att'y Gen. 304 (1918) (human body as "a kind of capital"), *quoted in* Sol. Op. 1384, 2 C.B. 71, 72 (1920). Both can be damaged or diminished. Both can generate income. Neither has basis. *See United States v. Garber*, 589 F.2d 843, 849-50 (5th Cir.) (Clark, J., dissenting), *rev'd*, 607 F.2d 92 (5th Cir. 1979).

The only apparent distinction between a physical injury and a nonphysical injury is the nature of the causal relation between harm and effect. The causal relation between physical intrusion and the resultant injury is often more readily perceived simply because there is tangible evidence showing the connection. This evidentiary difference, however, does not provide any principled means of separating the two types of injury and certainly has no relevance in taxation. From a tax perspective, this proposed distinction is plainly and simply arbitrary. This Court should reject the Commissioner's attempt to require the courts to make such unprincipled distinctions.

E. The inexorable consequence of the Commissioner's test is taxation of damages for physical injuries.

The Commissioner's theory regarding nonphysical injuries would logically lead to taxation of damages for physical injuries, reversing over seventy-five years of unbroken precedent and tax policy. The Commissioner's theory regarding taxation of damages for nonphysical injuries is simple. First, a back pay award for work performed represents an accession to wealth because it is a substitute for wages for services already provided, which would have been taxed as income if received currently

during employment.[10] SG Brief at 7. (The Commissioner also extends this reasoning to wages received for wrongful termination. *Id.* at 26 n.20.) Second, because such a recovery represents an accession to wealth, the exclusion of § 104(a)(2) would not be available under the Commissioner's test because the taxpayer could not establish that the recovery was a "reimbursement for a prior loss of personal 'capital.' " *Id.* at 14-15.

This logic cannot be limited to nonphysical injuries. It applies with equal force to a pianist or surgeon whose hands are injured, or a construction worker whose back is injured, or a schoolteacher whose voice is impaired. The lost wages in Rev. Rul. 61-1, 1961-1 C.B. 14, for example, would be taxable because they would have been taxable when earned.

Indeed, the logic of the Commissioner's position is not limited to back pay. Future earnings, like past earnings, are subject to tax when earned. Therefore, a recovery for loss of future earnings cannot be a tax-free return of capital. In sum, the logic of the Commissioner's circular reasoning has no stopping point except the full taxation of all damages measured by past or future loss of earnings. This reasoning would overturn almost seventy-five years of tax law excluding these recoveries from taxation.

The dramatic changes which would result from accepting the argument urged by the Commissioner have been considered and rejected by Congress. They should also be rejected by this Court.

---

10. This concept is discussed critically in Knickerbocker, *The Income Tax Treatment of Damages: A Study in the Difficulties of the Income Concept*, 47 Cornell L.Q. 429, 435 (1962). *Amici* believe that respondents' recovery does not represent back wages for the reasons stated *infra* p. 15 & n.16.

II. In applying section 104(a)(2), the Courts of Appeals and the Tax Court have looked to the nature of the claim asserted by the victim. They have made no distinction between economic and noneconomic damages from personal injuries.

A personal injury will often involve both economic consequences, such as lost wages, and noneconomic consequences, such as pain and suffering.[11] A surgeon whose hand is disabled or a baseball player whose back is injured will suffer both bodily pain and mental distress (noneconomic consequences) and lost wages (economic consequences). Valuation of a lost hand or a bad back can be so difficult that ultimately a victim may resort to the use of an economic yardstick to demonstrate the extent of the harm he has suffered, even though the noneconomic consequences may constitute the bulk of the harm.[12]

Congress apparently has recognized that a personal injury frequently entails both economic and noneconomic consequences and has written § 104(a)(2) to exclude both. Under the terms of § 104(a)(2), "*any* damages" are excluded so long as they are received on account of a personal injury (emphasis added).

11. The Courts of Appeals also use the term "nonpersonal consequences" to describe economic consequences and "personal consequences" to describe noneconomic consequences. *See, e.g., Bent*, 835 F.2d at 70; *Roemer*, 716 F.2d at 699. This brief uses the economic/noneconomic distinction merely to avoid confusion between a "personal injury" and its consequences, which can be both "personal" and "nonpersonal."

12. As the revenue solicitor noted over sixty years ago:

> The [personal] rights on the one hand and the money on the other are incomparable things which can not be placed on opposite sides of an equation. [Such a] personal right . . . is not assignable and not susceptible of any appraisal in relation to market values . . . .

Sol. Op. 132, I-1 C.B. 92, 93 (1922).

A. The Courts of Appeals and the Tax Court have concluded that a "nature of the claim" test implements the intent of section 104(a)(2).

In following the clear wording of the statute, the Circuit Courts and the Tax Court have unanimously concluded that § 104(a)(2) requires only that a court determine whether damages have been received on account of a personal injury. The fact that some of the damages may represent recoveries for economic consequences is of no import in assessing the taxability of damages. So long as the "nature of the claim" is that of a claim for personal injury, the resultant damages are excluded under § 104(a)(2).

An often-cited articulation of this "nature of the claim" test is in *Threlkeld*:

> Section 104(a)(2) excludes from income amounts received as damages on account of personal injuries. *Therefore, whether the damages received are paid on account of "personal injuries" should be the beginning and end of the inquiry.* To determine whether the injury complained of is personal, we must look to the origin and character of the claim . . . , and not to the consequences that result from the injury.

87 T.C. at 1299 (citations omitted) (emphasis added).[13] The Third, Sixth, Ninth, and Tenth Circuits have adopted this test, and the Fourth Circuit has adopted it in part.[14]

13. In *Threlkeld*, the Tax Court held that § 104(a)(2) excluded from gross income a malicious prosecution settlement attributable to injury to the taxpayer's professional reputation because the amount constituted damages received on account of personal injuries. *See* 87 T.C. at 1308.

14. *Pistillo*, 912 F.2d at 148 (3d Cir.); *Threlkeld*, 848 F.2d at 84 (6th Cir.); *Redfield v. Insurance Co. of N. Am.*, 940 F.2d 542, 544-45 (9th Cir. 1991); *Wulf*, 883 F.2d at 872-73 (10th Cir.). The Fourth Circuit, in *Thompson*, 866 F.2d at 712, seems to have adopted a bifurcated test. The *Thompson* court began with the proposition that the tax treatment of an award of liquidated damages and back pay received in a suit under Title VII and the Equal Pay Act turns on whether "the awards were received for personal

(continued...)

The courts' uniform adoption of a "nature of the claim" analysis is appropriate for four reasons. First, and most important, the test is consistent with the statute's clear reference to "any damages," and makes no distinction among the damages that may be received on account of personal injury.[15]

Second, the use of a "nature of the claim" test to determine the nature of damages received on account of litigation comports with this Court's holdings in the analogous area of the characterization of the consequences of litigation. In *Gilmore*, 372 U.S. 39, this Court held that the expense of defending a divorce suit was a nondeductible personal expense (rather than a deductible business expense) because its origin was personal rather than from the taxpayer's business. The Court expressly rejected a test based upon the consequences of the litigation:

> The principle we derive . . . is that the characterization, as "business" or "personal," of the litigation costs of resisting a claim depends on whether or not the claim *arises in connection with* the taxpayer's profit-seeking activities. It does not depend on the *consequences* that might result to a taxpayer's income-producing property from a failure to defeat the claim . . . . [S]uch a rule would lead to capricious results.

Id. at 48 (emphasis in original); *see Woodward v. Commissioner*, 397 U.S. 572, 577-78 (1970). Like the "consequences test" rejected in *Gilmore* and *Woodward*, the Commissioner's reliance here on the consequences of personal injury litigation would "encourage resort to formalisms and artificial distinctions." *Id.* at 577.

Third, the "nature of the claim" approach is analytically sound because it avoids confusion between the personal injury itself and its consequences. As the Ninth Circuit noted:

> Although there are different types of defamation actions (libel or slander) depending on the form of the defamatory statements, all defamatory statements attack an individual's good name. This injury to the person should not be confused with the derivative consequences of the defamatory attack, *i.e.*, the loss of reputation in the community and any resulting loss of income. . . . The *personal nature of an injury* should not be defined by its effect.

Roemer, 716 F.2d at 699 (footnote omitted) (emphasis added).

Finally, the "nature of the claim" test avoids confusion between what constitutes "damages" under § 104(a)(2) and how those damages, once found, are measured. Back pay or a similar economic yardstick is often simply used as a workable and expeditious means of measuring damages to a person's dignitary rights. Congress and the courts have used such measurements as a matter of convenience to protect rights that cannot be valued with any precision. As the Ninth Circuit has noted: "The *nonpersonal consequences* [*i.e.*, an economic yardstick] of a personal injury, such as a loss of future income, are often the most persuasive means of proving the extent of the injury that was suffered." *Roemer*, 716 F.2d at 699 (emphasis added).[16]

14.(...continued)
injuries through prosecution of a legal action based upon tort or tort-type rights." *Id.* at 711. That is the *Threlkeld* test. The court then determined that a sex discrimination claim is a tort-type action. *Id.* at 712. The entire award, therefore, should have been excluded under § 104 (a)(2). The court, however, then focused on the nature of the damages received and determined that the liquidated damages award was excludable as compensatory damages, but the back pay award was not excludable because it was in the nature of a breach-of-contract award. *Id.*

15. As noted *supra* pp. 6-7, in 1989 Congress did exempt punitive damages for nonphysical injury from § 104(a)(2). Punitive damages are not at issue in this case.

16. *See Threlkeld*, 848 F.2d at 84 (loss of future income "often the most persuasive means of proving the extent of the injury that was suffered" and "personal nature of an injury should not be defined by its effect"); *Bent*, 835 F.2d at 70 ("an award of damages for the violation of a constitutional right may be measured in whole or in part by the amount of lost wages"); *Metzger v. Commissioner*, 88 T.C. 834, 858 (1987), *aff'd without opinion*, 845 F.2d 1013 (3d Cir. 1988) (loss of income may merely be an evidentiary factor or the best measure of loss).

B. The Commissioner's proposed test is at odds with the statute and this Court's precepts in *Woodward* and *Gilmore*, and is based on an inapplicable theory regarding the taxation of damages.

The Commissioner disregards the clear terms of the statute that exclude "any damages" and instead proposes a test that distinguishes between economic and noneconomic consequences. According to the Commissioner, for nonphysical injuries, any receipt of back pay[17] (damages for economic consequences) represents an accession to wealth that should be taxed upon receipt by the tort victim. There is no basis in law or logic for such a distinction, and this Court should reject it.

First, there is no basis in the statute for distinguishing among different consequences from a personal injury. The statute states "any damages." It contains no qualification. Any further elaboration would make it " 'read like an insurance company's form [of] general release rather than a statute.' " *United States v. James*, 478 U.S. 597, 604 n.5 (1986) (quoting *James v. United States*, 760 F.2d 590, 604 (5th Cir. 1985) (Gee, J., dissenting)). Despite the long history of a fully inclusive definition of damages,[18] Congress has restricted § 104(a) only with respect to punitive damages for nonphysical injuries. Congress knows how to differentiate among types of damages for personal injury, yet it has declined to make the distinction the Commissioner now proposes.

---

17. Under the Commissioner's theory, "back pay" includes not only wages for work already performed, but also wages received for a wrongful discharge, where no work was performed. SG Brief at 18, 26 n.20.

18. The Commissioner has long held that § 104(a)(2) excludes recoveries attributable to back pay. Rev. Rul. 61-1, 1961-1 C.B. 14. The courts have also construed damages from personal injury to include a broad range of harms. *McDonald v. Commissioner*, 9 B.T.A. 1340, 1341 (1928) (excluding from gross income damages for breach of contract to marry, including "loss of station to which the marriage would have advanced plaintiff").

Moreover, although the Commissioner has repeatedly attempted to have courts accept a distinction between economic and noneconomic consequences, these attempts have met with a string of defeats. In *Roemer*, 716 F.2d at 697, the Ninth Circuit found no basis for distinguishing between economic recoveries (*e.g.*, lost wages) and noneconomic recoveries (*e.g.*, pain and suffering): Section 104(a)(2) applied even "when the predominant result of the injury is a loss of income." Following the decision in *Roemer*, the full Tax Court (by a 15-1 vote) and the Third, Sixth, and Tenth Circuits also rejected any distinction between economic and noneconomic consequences.[19]

In an attempt to find some support for his proposed distinction, the Commissioner argues that the taxability of recoveries should be determined under the principle that damages should be taxed in the same manner as the items they replace. SG Brief at 17. Back pay for lost wages, for example, would be taxable when received as damages because they would have been taxable when earned. This "substitution principle" is based on the theory that a payment received in settlement of a claim is simply a substitute for what the taxpayer would have received if there had been no dispute between the parties in

---

19. *Rickel v. Commissioner*, 900 F.2d 655, 661 (3d Cir. 1990) (nature of claim controlled; irrelevant whether damages, including back pay, compensate taxpayer for economic losses); *Byrne v. Commissioner*, 883 F.2d 211, 214 (3d Cir. 1989) ("relevant inquiry" in concluding settlement under New Jersey anti-discrimination law excludable "is whether the settlement was received on account of personal or non-personal injuries, not whether the damages compensate the taxpayer for economic losses"); *Bent*, 835 F.2d at 70 (3d Cir.) (settlement for First Amendment violation "admittedly" based on lost wages excludable; loss of future wages "often the most persuasive means" of proving extent of injury); *Pistillo*, 912 F.2d at 150 n.6 (6th Cir.) (specifically rejecting the Commissioner's proposed distinction in ADEA action between award of back pay and compensation for loss of human capital: "[W]hether [defendant] paid [the taxpayer] a portion of the settlement award to compensate him for pain and suffering or lost back pay is irrelevant to the § 104(a)(2) inquiry"); *Wulf*, 883 F.2d at 872-73 (10th Cir.) (award for lost wages -- including the portion of the recovery specifically representing back pay -- was excludable under § 104(a)(2) for First Amendment violation); *Threlkeld*, 87 T.C. at 1308 (damages received in settlement of malicious prosecution suit, including those for injuries to professional reputation, are excludable under § 104(a)(2)).

the first place. *See Church*, 80 T.C. at 1108; Fouts, *Payments Received in Settlement of Litigation and Claims*, 25 N.Y.U. Inst. Fed. Txn. 555, 556 (1966). This argument is flawed for two reasons. First, the argument begs the question. Lost wages may merely be a yardstick for other damages. *See supra* p. 15 & n.16. An award for an injury to dignitary interests does not constitute back pay. Second, § 104(a)(2) clearly constitutes an exception to the "substitution principle." *See Downey v. Commissioner*, 97 T.C. 150, 164 (1991) (§ 104(a)(2) "allows the exclusion for damages that are a substitute for amounts or items that otherwise would be taxable or would potentially produce taxable benefit, such as income lost as a result of a personal injury"). Even the Commissioner concedes that the exclusion of § 104(a)(2) applies to payments received in lieu of wages by virtue of physical injury. These wages, however, would also have been taxable when earned and would therefore be taxable under the substitution principle.[20]

III. The Commissioner's proposed approach, in which damages attributable to a nonphysical injury are excludable only where they *restore lost capital*, is conceptually misguided, is contrary to the statute, and renders section 104(a)(2) superfluous.

In his attempt to exclude respondents' awards from the scope of § 104(a)(2), the Commissioner introduces the concept that a recovery received on account of a nonphysical injury is excludable from income only if it compensates the taxpayer for

---

20. The Commissioner also protests that "tax-free" recoveries constitute an improper windfall where they would otherwise have been taxable. SG Brief at 22 n.16. The Commissioner's argument is not relevant in determining the scope of § 104(a)(2). First, victims of personal injury are accorded the exclusion of § 104(a)(2) because the award, even if proximately measured by back pay or lost wages, are to compensate for a personal injury, an interest for which there is no ready price. *See Pistillo*, 912 F.2d at 150. Second, there is no reason to believe that Congress has not maintained the exclusion out of a sense of compassion for the victims of personal injury. *Roemer*, 716 F.2d at 696 n.2.

a prior loss of "personal capital." SG Brief at 14. Because a damage award measured by back pay purportedly would not constitute such a recovery, the amount would be taxable. *See* SG Brief at 20-21, 26 n.20. This Court should reject the Commissioner's proposed approach.

A. The Commissioner's definition of "personal capital" is conceptually misguided.

The Commissioner concedes that damages received on account of *physical* injuries, even when measured by back pay, constitute a return of personal capital and are not taxable. SG Brief at 21 n.16. The Commissioner then argues that damages received on account of *nonphysical* injuries, when measured in precisely the same fashion, cannot constitute a return of personal capital. SG Brief at 26 n.20. This position is ill-conceived and conceptually misguided. A person's intellect, integrity, self-respect and good name are as much "personal capital" as are arms and legs and good health. All are essential aspects of a human being.[21]

The issue is not whether income can be generated from such personal capital. Nor is the issue whether such income, when generated, can be taxed. The issue is whether damages received from an injury to such personal capital are or should be taxed and, more specifically, in this case, whether such damages should be taxed when the injury was caused by years of invidious discrimination based upon the sex of the injured party.

---

21. *See* William Shakespeare, *Othello*, act 3, sc. 3:
Good name in man and woman, dear my lord,
Is the immediate jewel of their souls:
Who steals my purse steals trash; 'tis something, nothing;
'Twas mine, 'tis his, and has been slave to thousands;
But he that filches from me my good name
Robs me of that which not enriches him,
And makes me poor indeed.

It is undisputed that the tax law does not and should not tax the possession or enjoyment of "personal capital" such as good health or a fine intellect. *See Hawkins*, 6 B.T.A. at 1025. The Commissioner's own rulings have long recognized this principle. From 1918 to the present, the IRS has steadfastly maintained that damages received on account of a personal injury should not be taxed because they are a return of personal capital. *See* Sol. Op. 1384, 2 C.B. at 72 (citing 31 Op. Att'y Gen. 304 (1918)); Rev. Rul. 61-1, 1961-1 C.B. 14; Rev. Rul. 85-143, 1985-2 C.B. 55 (citing rulings).

While these rulings have been couched in technical tax terms such as "basis" and "return of capital," as Justice Frankfurter acknowledged in *United States v. Kaiser*, 363 U.S. 299, 311-12 (1960) (Frankfurter, J., concurring), these rules are technically suspect but unquestionably correct:

> The principle at work here [in the Commissioner's holdings in Sol. Op. 1384 and Sol. Op. 132, I-1 C.B. 92 (1922)] is that *payment which compensates for a loss of something which would not itself have been an item of gross income is not a taxable payment.* . . . If a capital asset is sold for no more than its basis there is no taxable gain. The result, then, is the same if it is destroyed and there is paid in compensation no more than its basis. There are, to be sure, difficulties, not present where ordinary assets are involved, in applying this principle to compensation for the loss of something which has no basis and which is not ordinarily thought of as a capital asset, such as health or life or affection or reputation. . . .
>
> [In recoveries for personal injury,] the thing lost and compensated for was not an item of taxable income, but an aspect of capital or analogous to capital, which obviously would not have been included in gross income had it been retained.

Id. (emphasis added).[22]

The Commissioner's rulings cited above are technically questionable because in reality such "personal capital" has no measurable basis. Because "personal capital" has no basis, theoretically any amount received as compensation for its loss is technically "gain." The rulings, however, are also unquestionably correct in excluding such theoretical gain from taxation. They are correct for one simple and overriding reason: Any tax system that reached a different result would be one that placed the technical theory of gain and loss and income above basic concepts of value and human dignity.

B. The Commissioner's proposed test has no basis in the statute.

The Commissioner's "return of capital" theory also suffers from the flaw that it has no basis in the statute. In fact, there is not one shred of evidence in the statute that Congress intended to limit the term "any damages" to awards that constitute a return of capital. Neither the statute itself nor the legislative history refers to such a concept. Moreover, there are substantial reasons to believe that Congress did *not* intend that the courts read a return of capital qualification into § 104(a)(2). Such a reading would render § 104(a)(2) a nullity and introduce a complex and difficult test into tax administration.

---

22. Under a traditional application of the return of capital theory, *all* personal injury recoveries (which are by definition compensatory only, *Glenshaw Glass*, 348 U.S. at 432 n.8) do not constitute accessions to wealth. The Commissioner's distinction between "return of capital" and "gain or profit" would therefore have no application for compensatory damages, whether those damages compensated for economic or noneconomic consequences. It is also arguable that, regardless of considerations of tax theory, Congress has accepted the Commissioner's *de facto* exclusion of these items from income through continued congressional acquiescence. *See* Boris I. Bittker & Martin J. McMahon, Jr., *Federal Income Taxation of Individuals* ¶ 3.6, at 3-20 (1988) (arguing for such congressional acquiescence).

C. The Commissioner's argument renders section 104 (a)(2) superfluous.

The Commissioner argues that, for nonphysical injuries, § 104(a)(2) should exclude only those recoveries that represent a "return of capital" to the taxpayer.[23] Acceptance of the Commissioner's "return of capital" argument reads § 104(a)(2) out of the Code. This Court should reject it.

The Commissioner's position could not be more clear. According to his argument, respondents must establish that "the recovery is reimbursement for a prior loss of personal 'capital' . . . and does not represent gain or profit that 'instead add[s] to [their] wealth.' " SG Brief 14-15 (citations omitted). It is equally clear, however, if a taxpayer can establish that a reimbursement is a return of capital, the amount does not constitute income in any event and would not be taxable under the Sixteenth Amendment. 31 Op. Att'y Gen. 304; Sol. Op. 132, I-1 C.B. at 93; *see Doyle v. Mitchell Bros. Co.*, 247 U.S. 179, 185 (1918) (return of capital not income).

If the amounts received constitute a "return of capital," then under this Court's holding in *Doyle*, the amounts do not constitute income and by definition they are not taxable under the Sixteenth Amendment. The Commissioner, however, would limit the exclusion of § 104(a)(2) to precisely those recoveries. At least with respect to nonphysical injuries, the Commissioner's test would read § 104(a)(2) out of the Code. This Court has long held that an interpretation of a statute that renders the statute a nullity cannot be adopted. *Singer v. United States*, 323 U.S. 338, 344 (1945) (Court avoids interpretation that makes provision redundant); *Bernier v. Bernier*, 147 U.S. 242, 245 (1893) (statutes must be interpreted so that one section "will not defeat or destroy another, but explain and support it").

23. Relying on footnote 8 of *Glenshaw Glass*, the Commissioner argues that the Court "did not reject" his position, taken since 1918, that recoveries for personal injuries do not constitute income to the extent they "correspond to a return of capital." SG Brief at 13.

Because acceptance of the Commissioner's argument would have this precise effect, that construction should be rejected.

D. The Commissioner's test relies on a theory that has no discernable scope.

The Commissioner's test also suffers from the arbitrary distinction between what constitutes a "return of capital" *versus* "gain or profit." The Commissioner argues that recoveries of back wages on account of a physical injury are a return of capital. SG Brief at 21 n.16. But the Commissioner insists that recoveries for back wages on account of a nonphysical injury are not a return of capital. SG Brief at 26 n.20. These two situations, however, are indistinguishable. In both cases the victims are prevented from earning their wages either because (for example) the employer's machinery tortiously injured the employee or because (for example) the employer discriminatorily fired the employee. There is no discernable reason to conclude that human capital includes the ability to obtain an income stream in the former instance and not in the latter. The Commissioner attempts to distinguish the two tort victims by arguing that back wages for nonphysical injuries represent wages that should have been paid but were not. This distinction, however, provides no guidance regarding the contours of "human capital" since both tort victims cannot work and do not receive wages.

Nor do cases or rulings illuminate the inquiry. Because of the novelty of the Commissioner's test, no court has ever examined this issue in determining the scope of § 104(a)(2). In fact, the only guidance available predates *Glenshaw Glass* by at least twenty years. *See McDonald v. Commissioner*, 9 B.T.A. 1340, 1341 (1928) (damages for breach of contract to marry); *Hawkins*, 6 B.T.A. at 1025 (defamation); Sol. Op. 132, I-1 C.B. at 93 (defamation, alienation of affections, surrender of a child); 31 Op. Att'y Gen. 304 (personal injury). The Commissioner's test is unwarranted under the statute and, because of the lack of definiteness of "human capital," injects vast uncertainty into tax administration. This Court should reject it.

IV. Amounts received by respondents in settlement of their Title VII suit are excludable from income under section 104(a)(2).

As discussed *supra* pp. 13-15, the Tax Court and the Courts of Appeals have uniformly based the tax treatment of damages received through suit or settlement on the nature of the claim giving rise to the awards. Because suits brought under Title VII allege a personal injury within the meaning of § 104(a)(2), any damages received through prosecution or settlement of a Title VII action fall squarely within the exclusion. Because the back pay awards received by respondents are "damages received . . . on account of personal injuries" within the meaning of § 104(a)(2), the entire award is excludable from gross income.

A. A violation of Title VII results in "personal injuries" within the meaning of section 104(a)(2).

Although § 104(a)(2) does not define the term "personal injuries," the Tax Court and the Courts of Appeals have consistently interpreted it to have two components. First, to qualify as an injury, the alleged harm must give rise to "some sort of tort claim against the payor." *Glynn v. Commissioner*, 76 T.C. 116, 119 (1981); *see Pistillo*, 912 F.2d at 148; *Rickel*, 900 F.2d at 658. Second, a "personal" injury requires the Court to distinguish between personal and nonpersonal injuries. *Roemer*, 716 F.2d at 697 ("relevant distinction that should be made is between personal and nonpersonal injuries"); *Thompson*, 866 F.2d at 711 (same). An injury to property, for example, would be a "nonpersonal" injury. Because a claim for violation of Title VII meets both requirements, it is a claim on account of "personal injuries" within the meaning of § 104(a)(2).

A claim of employment discrimination implicates a tort or tort-type right in either of two ways. First, it may allege a breach of duty that "arises by operation of law," "independent

of any duty an employer might owe his employee pursuant to an express or implied employment contract." *Byrne v. Commissioner*, 883 F.2d 211, 215 (3d Cir. 1989) (violation of FLSA's duty not to discriminate against whistleblowers); *see Pistillo*, 912 F.2d at 149 (violation of ADEA's duty not to discriminate on the basis of age); *Rickel*, 900 F.2d at 662 (same); *Thompson*, 866 F.2d at 712 ("tort action is one for 'a direct invasion of some legal right of the individual' independent of contract") (quoting Black's Law Dictionary 1335 (5th ed. 1979)). An employment discrimination action also vindicates a tort-type right when it alleges "any invasion of the rights that an individual is granted by virtue of being a person in the sight of the law." *Threlkeld*, 87 T.C. at 1308; *see Bent*, 835 F.2d at 69 (42 U.S.C. § 1983 (1988) violation; invasion of right to freedom of speech); *Wulf*, 883 F.2d at 873 (same).

An action based on Title VII falls squarely within either definition. A claim under Title VII seeks to remedy an alleged violation of the employer's statutory duty not to discriminate on the basis of race, color, religion, sex or national origin, a duty independent of any contractual duty an employer might owe its employees. 42 U.S.C. § 2000e-2 (1988); *Thompson*, 866 F.2d at 712 ("right to be free from unreasonable gender discrimination is a personal right" independent of contract). Similarly, it has long been held that discrimination on the basis of sex, race, or national origin results in an invasion of the individual rights and dignity of the person. *See, e.g., Goodman v. Lukens Steel Co.*, 482 U.S. 656, 661 (1987) (race discrimination, challenged under 42 U.S.C. § 1981 (1988), "is a fundamental injury to the individual rights of a person"); *Curtis v. Loether*, 415 U.S. 189, 195 n.10 (1974) (analogizing race discrimination to a "dignitary tort"); *Price Waterhouse v. Hopkins*, 490 U.S. 228, 264 (1989) (O'Connor, J., concurring) (violation of Title VII, "the statutory employment 'tort,' " similar to common law tort). Respondents' Title VII claim alleging unlawful gender discrimination, therefore, seeks vindication of tort-type rights.

A violation of Title VII also results in an injury to the person of the claimant. Courts have frequently noted the physical and psychological injuries resulting from workplace dis-

crimination on the basis of sex, race or national origin. *See, e.g., Zabkowicz v. West Bend Co.*, 789 F.2d 540, 542 (7th Cir. 1986) (doctor's diagnosis of " 'gastro-intestinal disease due to [sexual] harassment at work' "); *Brooms v. Regal Tube Co.*, 881 F.2d 412, 417 (7th Cir. 1989) (severe, debilitating depression caused by sexual and racially motivated harassment in workplace). Congress, too, has recognized that personal injuries result from workplace discrimination:

> Victims of *intentional* discrimination often endure terrible humiliation, pain and suffering while on the job. This distress often manifests itself in emotional disorders and medical problems, which in turn cause victims of discrimination to suffer substantial out-of-pocket medical expenses and other economic losses as a result of the discrimination . . . . The Committee intends to confirm that the principle of anti-discrimination is as important as the principle that prohibits assaults, batteries and other intentional injuries to people.

H.R. Rep. No. 40, 102d Cong., 1st Sess., pt. 1 at 14-15 (1991) (emphasis in original). These injuries to the person of the victim are clearly distinct from nonpersonal injuries to the victim's property rights or contract rights. They also are distinct from the nonpersonal consequences of the injury, such as loss of income. Because a suit brought under Title VII seeks to vindicate tort-type rights, the violation of which causes physical and psychological harm to the claimant, respondents' claims of gender discrimination under Title VII are "personal injuries" within the meaning of § 104(a)(2).[24]

---

24. Recently, in *Owens v. Okure*, 488 U.S. 235 (1989), this Court held that the general limitations statute for personal injury actions applies to claims brought under 42 U.S.C. § 1983, including a claim for gender discrimination under the Equal Protection Clause. In so holding, this Court stated that § 1983 " 'confer[s] a general remedy for injuries to personal rights' " and that " '§ 1983 claims are best characterized as personal injury actions.' " *Id.* at 240 (citations omitted). *See Goodman v. Lukens Steel Co.*, 482 U.S. 656 (1987) (a violation of § 1981 is a "tort-type" injury for purposes of determining which (continued...)

B. Title VII back pay awards are damages within the meaning of section 104(a)(2).

Section 104(a)(2) excludes "any damages" from gross income. The regulations specify that "[t]he term 'damages received' " means "an amount received . . . through prosecution of a legal suit or action based upon tort or tort-type rights, or through a settlement agreement." Treas. Reg. § 1.104-1(c).

One court has held that an award of back pay received through the prosecution of a Title VII action, being an equitable remedy, is not "damages" within the meaning of § 104(a)(2). *Sparrow v. Commissioner*, 1991 U.S. App. LEXIS 27991 (D.C. Cir. Nov. 26, 1991). In construing § 104(a)(2), however, the Commissioner's regulations define the term "damages" to include "*an* amount" received on account of personal injuries, apparently eliminating any distinction between damages in equity and at law.[25] Treas. Reg. § 1.104-1(c) (emphasis added). The plain meaning of the term "damages" also does not support a distinction between legal and equitable relief. *See* Black's Law Dictionary 351 (5th ed. 1979) ("a pecuniary compensation . . . which may be recovered in the courts"). The structure of § 104(a) also belies any distinction between equitable and legal damages. Excludability turns on the source of the amounts received, not their nature. *See* I.R.C. § 104(a)(1) ("amounts received under workmen's compensation"); *id.* at § 104(a)(3) ("amounts received through accident or health insurance"); *id.* at § 104(a)(4) ("amounts received as a pension [or] annuity"); *id.* at § 104(a)(5) ("amounts received . . . as disability income").

24.(...continued)
state statute of limitations applies). Similarly, Title VII claims seek relief for injuries resulting from discrimination -- personal injuries for purposes of § 104(a)(2). *Metzger*, 88 T.C. 834 (claims under §§ 1981 and 1983 and Title VII are actions for a personal injury).

25. This issue is discussed at greater length in respondents' brief.

Other provisions of the Code explicitly refer to equitable and legal actions when appropriate. *See, e.g.*, I.R.C. § 6305(b) (1989) (removing from jurisdiction of United States courts "any action, whether legal or equitable" brought to review certain tax collections). Absent any evidence to the contrary, the plain meaning of the term "damages" should prevail and, therefore, § 104(a)(2) applies to back pay awards under Title VII despite their equitable nature. *Escondido Mutual Water Co. v. LaJolla Band of Mission Indians*, 466 U.S. 765, 772 (1984) ("[s]ince it should be generally assumed that Congress expresses its purposes through the ordinary meaning of the words it uses, we have often stated that '[a]bsent a clearly expressed legislative intention to the contrary, [statutory] language must ordinarily be regarded as conclusive' ") (citations omitted).

CONCLUSION

The opinion of the Sixth Circuit Court of Appeals should be affirmed.

Respectfully submitted,

C. CABELL CHINNIS, JR.
(Counsel of Record)
ELAHNA R. STROM
PHILIP L. GORDON
ELIZABETH B. DIXON
JULIE E. BARLAND
LATHAM & WATKINS
1001 Pennsylvania Avenue, N.W.
Washington, D.C. 20004
(202) 637-2200

STEVEN R. SHAPIRO
ISABELLE KATZ PINZLER
AMERICAN CIVIL
LIBERTIES UNION
FOUNDATION
132 West 43 Street
New York, New York 10036
(212) 944-9800

ALISON C. WETHERFIELD
MARTHA F. DAVIS
NOW LEGAL DEFENSE
AND EDUCATION
FUND
99 Hudson Street
New York, New York 10013
(212) 925-6635

JULIUS L. CHAMBERS
CHARLES STEPHEN RALSTON
NAACP LEGAL DEFENSE
AND EDUCATIONAL
FUND, INC.
99 Hudson Street
New York, New York 10013
(212) 219-1900

Dated: December 20, 1991